GOLD SUPPLY AT THE CLOSE OF THE WAR—DISCUSSION

Murray S. Wildman.—I find myself in accord with most conclusions reached by Mr. Roberts' paper. The annual product of the mines, supplemented by diversion from the arts, and this condition aggravated by enormous issues of paper, are increasing the world's money supply more rapidly than population or commodities are increasing.

This menace of gold bodes ill for all commercial countries, but more particularly for the neutral nations when long-war conditions are in mind. Assuming that the gold standard remains intact and that belligerents resume specie payments where they are now suspended or increase reserves where the paper is convertible, there will be an immediate movement of gold from America and other neutral countries which will give a shock to our credit structure. However, this outward movement will, in my opinion, be of short duration and extent, and we shall soon receive back and continue to hold more than our share of the world's gold supply. I think this proposition can be conclusively demonstrated.

In order to present the argument for this view it will be convenient to speak of a normal distribution of gold. By this I mean the relative per-capita circulation which existed prior to the war. Let us suppose that we had in this country in 1914 one ounce of gold per capita, Great Britain half an ounce, France three quarters and so on. It matters not how this distribution came about save that it resulted from long monetary and banking habits and trade relations. When any sudden increase of supply would take place, the new gold would spread over the world by additions to the stock of all communicating countries, but the old normal distribution would not be changed. Instead of one ounce, one half ounce, and three quarters, we should have one plus, one half plus and three quarters plus. The old *ratios* would remain unchanged.

But the war has changed this normal distribution so that after peace comes and a short period of readjustment has elapsed a different series of ratios will be found to maintain and the new ratios with larger terms for the neutral countries will be relatively permanent.

The first disturbance of the normal distribution came when governments at war began to issue paper. Whether convertible or not this paper displaced gold, cheapened it, invited the import of goods, followed by the export of gold. A characteristic of a paper circulation is that it tends to become permanent. A shift in the distribution of gold caused by an increase of paper also tends to be permanent.

A second cause for a new normal distribution is found in new credit and trade relations. One cannot deal with this subject in a few minutes, save in a most superficial way, and I shall try not to mention any changes except those that are most obviously certain to occur.

Before the war we were a debtor nation by a large amount. We must annually export gold or goods in excess of our imports. If foreign prices on exportable goods were higher than ours we sent goods. If not we sent gold and continued to send gold until our price was lower than the foreign price. Of course it was not general prices but particular prices of exportable goods which determined whether goods or gold would be shipped. Suppose that all exportable commodities be represented by one such as wheat. If the Liverpool price of wheat was high enough we obtained the necessary exchange by a shipment of wheat, but if their price was too low we shipped gold, and gold would continue to go abroad until our general price level—including the price of wheat—fell low enough to export wheat rather than gold. By this process of adjustment our normal distribution of gold was established and maintained.

After the war, if we remain neutral to the end, we shall find ourselves in one or two situations; we shall remain a debtor nation with a small debt and small annual charge, or else, if the war continues long, we shall be a creditor nation with an annual credit balance. In the first case our annual loss of goods or gold will be less. In the second case there will be an annual gain of gold or goods instead of a loss. The net result will be that our price of importable goods must be higher than that prevailing abroad or else gold will come to us until our price level is raised to the point of profitable importation.

In objection to this view it may be urged that when we talk of exports and imports we are talking of different goods, and that a high foreign price of wheat is consistent with a low foreign price of coffee, and that the old normal distribution of gold may be maintained by merely reducing our export of wheat as our annual interest charge is reduced, or increase our import of coffee if an annual credit balance should appear.

This objection would be sound if coffee and wheat were interchangeable in consumption, but they are not interchangeable nor are imports and exports generally interchangeable. In this case, as in so many, we must assume that our habits of consumption remain unchanged, at least for a considerable period. If we admit that assumption we cannot avoid a continuously greater stock of gold and a permanently

higher price level than we should have experienced in our traditional status as the world's greatest debtor nation.

I can think of no legislative measure likely to counteract this tendency. Protective duties might aggravate it. In the course of time there would be a relatively larger home consumption of goods which formerly entered into our export trade but to which foreign markets have become less hospitable. There would be a tendency to increase the variety and range of imported goods if they are allowed to enter freely, but the excess gold supply already reached would hardly be diminished.

E. M. Patterson.—With most of the statements made by Mr. Roberts there is little ground for disagreement. That we are experiencing a very great influx of gold, a supply that is secured from the mines and from the circulation of the leading belligerent countries, is well known. Because the belligerent countries have many selfish reasons for maintaining the gold standard it seems probable that gold will not be demonetized. There will be strong influences operating after the war that will tend to take from us at least a part of our large supply of gold, but the withdrawal of this gold is something that should not be looked upon with dread provided it can be kept under proper control.

The problem of controlling this gold movement is one that will differ only in degree from the problems of gold control in ordinary times. In the past the United States has probably been the freest gold market in the world. We have been unable to attract gold as we need it from other countries if at the same time they were desirious of retaining it. When they wished to take it from us we have been unable to prevent the export. This was illustrated in the fall of 1913. At that time we were feeling some strain in our markets and needed to import gold for relief. An attempt on our part to do so was met by an increase in the discount rate of the Bank of England and the shipment was canceled. At the same time Canada was exporting large quantities of gòods and securities. Her bankers sold in New York the London exchange drawn against these exports and then withdrew gold from New York to Montreal. We were unable to prevent the exportation of this gold and at the same time could import none.

There will be two main influences on which to rely in the future. The first is the aid and coöperation of our banks. Doubtless the

need for control will be fully appreciated by them and considerable unity of action may be secured. Particularly will they be able to rely on their holdings of short-time foreign government securities, of which there have been accumulated a large amount, approximating at the present time $2,000,000,000. As market conditions warrant and as these mature, it is probable that our banks will as a matter of self-interest dispose of these holdings, refusing to renew them at maturity in case such renewal would mean the withdrawal of unduly large amounts of gold from the United States.

To a considerable extent, however, we must hope for assistance from the federal reserve system. One may agree with the assertion that this system is not yet working as effectively as the foreign central banks and at the same time acknowledge that its influence is growing and that its possibilities are very great. Some of the phases of the system that frequently escape notice and that may be of advantage in emergencies are the following:

1. The rediscount rates of the various reserve banks may be altered. If the demand for funds is particularly heavy and results in a considerable amount of pressure on the reserve banks and on their supplies of gold, these discount rates may be raised and the raid on the reserve banks' gold holdings checked. How effective this will be in practice remains to be seen, as the reserve banks have as yet had no opportunity to use their influence in this direction.

The significance of this control through the discount rate is determined largely by a consideration of the amounts of gold that will be in the hands of the federal reserve banks and hence subject to their control. This gold is of two kinds. There is first the gold held in the reserve of the federal reserve banks as a part of their assets. In the second place there is the gold that has been accumulated now to the extent of about $280,000,000 in the hands of the federal reserve agents behind the federal reserve notes, of which there are over $300,000,000 outstanding. These two supplies of gold at the present time total between $700,000,000 and $800,000,000. This is no small sum when one stops to realize that the reserve banks have been in operation only about two years. Under the circumstances one might wish that it were larger but it is large enough to be of very considerable importance.

2. The reserve banks have accumulated considerable holdings of United States bonds and notes and also are in a position in time of stress to sell these bonds and notes, as well as some of their holdings of

municipal warrants, without danger of much loss through depreciation. This will tend to tighten the money market, give to the reserve banks more control over funds, and is a method that is resorted to frequently by the leading central banks of European countries.

3. The reserve banks may also borrow gold on the market, offering some of their bonds, notes, and warrants as collateral security. This practice also is followed by central banks abroad.

4. Through their participation in foreign exchange transactions the reserve banks are coming into possession of considerable amounts of credit abroad. The acquisition of these holdings will tend to lessen the importation of gold now and at the same time will furnish to our federal reserve banks accounts against which they can later sell exchange if they desire to influence the exchange rates and keep them below the gold export point. Just how important this control will become remans to be seen, but it is worth while to note that an interesting beginning has been made by the designation of the Bank of England as the English agency of the Federal Reserve Bank of New York. It is also reported that similar arrangements are to be made with the Bank of France, the Bank of Germany, and other institutions.

5. Finally there may be mentioned the possibility that a mere disapproval by the Federal Reserve Board, a disapproval expressed or merely implied, may have considerable influence. It is well known that such disapproval is a very potent influence in Germany and in certain other countries. If the Reichsbank or German government considers it inexpedient for gold to leave the country, gold does not go, even though the rate of exchange would seem to warrant an export movement. How soon, if at all, our Federal Reserve Board will acquire a similar influence over gold shipments is uncertain. It is interesting to observe, however, that quite recently a mere expression of disapproval by the Federal Reserve Board caused our bankers to change their plans for investing their funds in English Treasury bills. It is a matter of great interest and importance that our Federal Reserve Board has in so short a time acquired a position of such influence.

How effective any or all of these devices may be it is impossible to forecast. That the Federal Reserve Board is aware of such weaknesses as may exist, is evidenced by the various requests to Congress for amendatory legislation by which the ability of the reserve banks to secure and control the gold supply will be increased. Some of this legislation was passed at the last session of Congress and it is hoped that still more progress will be made at this one.

Don C. Barrett.—Mr. Roberts holds that much gold will flow from us when the war closes and views such prospect with equanimity. Other gentlemen hold that we may not lose much gold and are inclined to feel disturbed at the thought of any considerable outflow. The question is one of relative level of prices. Whatever may be the redistribution of the world's gold supply in the long run, it seems probable that we shall lose a very considerable quantity temporarily at least. One of the chief reasons is that the industrial organization of the belligerent countries is in a markedly more abnormal state than that in which American organization finds itself. English and European industries have been almost completely transformed for the purpose of producing war materials, while our industries, in spite of the fact that we are exporting large quantities of munitions, are for the most part organized for the production of the same kinds of goods as they will be called upon to produce after peace is declared. The scale of readjustment in the belligerent countries will therefore be much greater than with us. The credit operations of various sorts which are now supporting their industries must be weakened and materially diminished during the period of enforced readjustment, and especially in the initial stages of readjustment. The withdrawal of this supporting credit structure will cause a decline, more or less serious, in their price level. This decline is likely to take place in spite of efforts which different governments may exert to support business interests in order to prevent it. Since industrial readjustment in America will be on a relatively small scale, credit operations supporting industry will be interfered with relatively less and the decline in the American price level will, for some time at least, be relatively slight. The consequent tendency will be for gold to flow from us in considerable amounts—eventually of course inducing a decline in prices.

Whether this outflow of gold will bring a crisis in American business circles depends upon the attitude and action of our business men. If they are unduly optimistic and attempt to maintain extended credits, they are liable to encounter much difficulty. If they are cautious as to the future and draw in their credit operations, they will probably escape any serious crisis—precisely as did business men at the close of the Civil War. In that earlier event most men, being sure a crisis was coming with the declaration of peace, prepared for it by diminishing their credits and holding to conservative business; and then naturally, as a consequence, the crisis never came. History may repeat

itself and business men may not be injured by an outflow of gold to anything like the extent many of them now anticipate. The steadying influence of the federal reserve system may promote this outcome.

MR. ROBERTS.—I did not mean to say that I thought gold would go out until we had lost all that had been acquired during the war. I think there will be a redistribution of gold under the influences which normally give each country a share proportionate to its wealth, a share of the world's trade, banking customs, etc. I think our normal share will be greater after the war than it was before, but I do not think it will be anything like great enough to retain all the gold we have received.

Answering an inquiry, I would say that demand and supply undoubtedly have an immediate influence upon prices. Under this influence prices are expected to fall after the war. At a lower level of prices, and with a reduction in the volume of business, less money and credit will be required, and we shall not use the amount of gold we have received. If we do not need it and cannot use it, I do not think we shall retain it. The point I have endeavored to make is that the amount of gold which we shall have at the end of the war, if actually absorbed and in use, would require a level of prices impossibly high. Other influences will dominate and compel a lower level of prices; hence, in my opinion, a considerable portion of our newly acquired gold will be naturally released for transfer to the countries which need it more than we do.

It is true that movements of this kind do not work out in experience as smoothly as in theory. Tariffs may prevent the importation of goods, and the inexperience and hesitation of our people as purchasers of foreign securities may retard the movement of securities. I think, however, that means will be found to transfer a considerable amount of gold.